Exhibit L

B-Book: How Forex Brokers Manage Their Risk

When the retail forex broker takes the opposite of a customer's trade, it can choose to **ACCEPT the market risk or TRANSFER it to another market participant**.

If a broker chooses to accept the market risk, when the trade is executed, it is called "**B-Book execution**".

"B-Book execution" is just a fancy phrase for **taking the opposite of your trade**.

Your trade can also be described as being "**B-Booked**".

And since the broker has taken on risk, here are other examples of industry jargon:

- The risk has been "**internalized**".
- The risk has been "**warehoused**".

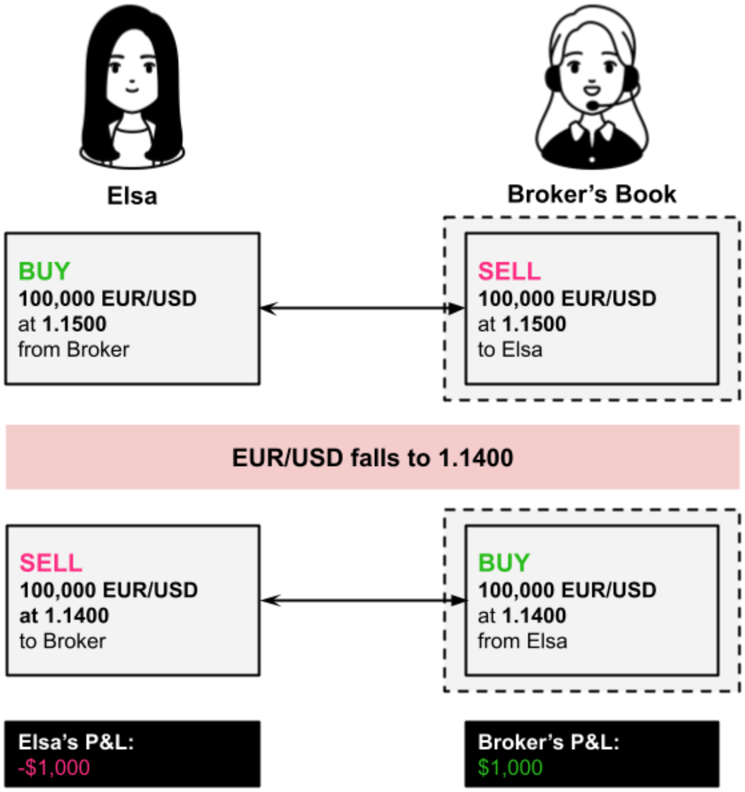
Because the broker has decided to "hold" the risk, it has kept the risk for itself ("internalized") and stored the risk ("warehoused").

Not sure if market risk appreciates being objectified. 😂

Depending on whether the market moves for or against the broker, **accepting market risk can either be good OR bad for the broker**.

Let's look at an example of each.

B-Book Order Execution Example #1: Broker Wins



In the example above, Elsa went long 100,000 EUR/USD at 1.1500. Her broker "B-Booked" (took the opposite of) the trade and is short 100,000 EUR/USD.

EUR/USD falls to **1.1400**.

Elsa can't take the pain any longer and closes her position by selling 100,000 EUR/USD at 1.14000.

She ends up with a **$1,000 loss**

```
P&L = (Exit Price - Entry Price) x Position Size
-1,000 = ((1.1400 - 1.1500) x 100,000)
```

On the other hand, the broker ends up with a **$1,000 profit**.

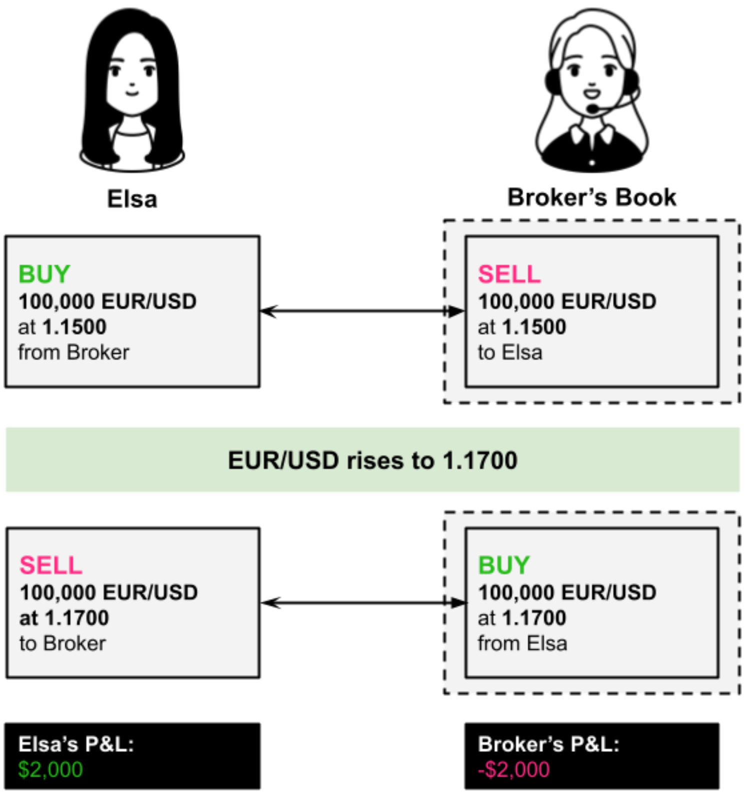
```
P&L = (Entry Price - Exit Price) x Position Size
1,000 = ((1.1500 - 1.1400) x 100,000)
```

In this scenario, for accepting the market risk, the broker was rewarded with a **PROFIT**.

It was a positive outcome.

B-Book Order Execution Example #2: Broker Loses

Let's now take a look at what happens when the **market moves AGAINST the broker**.



In the example above, Elsa went long 100,000 EUR/USD at 1.1500. Her broker "B-Booked" (took the opposite of) the trade and is short 100,000 EUR/USD.

EUR/USD rises 200 pips to 1.1700.

Elsa decides to take profit and closes her position by selling 100,000 EUR/USD at 1.17000.

She ends up with a **$2,000 profit**

```
P&L = (Exit Price - Entry Price) x Position Size
2,000 = ((1.1700 - 1.1500) x 100,000)
```

On the other hand, the broker ends up with a **$2,000 loss**.

```
P&L = (Entry Price - Exit Price) x Position Size
-2,000 = ((1.1500 - 1.1700) x 100,000)
```

In this scenario, for accepting the market risk, the broker suffered a **LOSS**.

It was a negative outcome.

Here's a summary of how a B-Book broker benefits depending on the outcome of a trade:

Customer's Trade	Broker's Order Execution	Benefit
Win	B-Book (Accept risk)	Customer's gain is broker's loss
Lose	B-Book (Accept risk)	Customer's loss is broker's gain

Potential Conflict of Interest

There is a lot of controversy with B-Book execution.

Since your broker makes money if you lose money, there exists a potential conflict of interest.

It creates the potential for the broker to do "bad" things to increase the chances that your trades lose.

This causes traders to be concerned about shady behavior from brokers who don't want their customers winning.

We won't go into examples of broker shadiness just yet since the focus of this lesson is **how forex brokers manage their market risk** (not how shady brokers take advantage of their customers).

For now, just know that when a forex broker chooses to **accept market risk** ("B-Book execution"), a major downside to doing this is that a potential conflict of interest does exist between a broker and its customers.

In the next lesson, we'll learn another way that a broker manages market risk: **by *transferring* it** (or "A-Book execution").

Next Lesson
A-Book: How Forex Brokers Manage Their Risk

What to Read Next...

What is ICT Trading in Forex?

Play of the Day Recaps: October 23 – 27, 2023

a day ago

FX Weekly Recap: October 23 -27, 2023

3 days ago

"I always define my risk, and I don't have to worry about it."

- Tony Saliba

B-Book: How Forex Brokers Manage Their Risk - BabyPips.com

Contribute 💰

babypips

Babypips helps new traders learn about the forex and crypto markets without falling asleep.

We introduce people to the world of trading currencies, both fiat and crypto, through our non-drowsy educational content and tools. We're also a community of traders that support each other on our daily trading journey.

Privacy Policy Risk Disclosure Terms of Use Do Not Sell My Personal information Change Consent